

Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author: Correa Analyst: Jeff Garnier Bill Number: AB 2268Related Bills: See Leg. History Telephone: 845-5322 Introduced Date: February 24, 2KAttorney: Patrick Kusiak Sponsor: Governor's Office**SUBJECT:** Long-Term Care Caregiver CreditSUMMARY

This bill would provide for a \$500 non-refundable credit to taxpayers who are eligible caregivers for each applicable individual in need of long-term care. An applicable individual may be the taxpayer, spouse of the taxpayer or a qualifying (under this bill) dependent who has been certified to have long-term care needs.

EFFECTIVE DATE

This bill would be effective immediately upon enactment and operative for taxable years beginning on or after January 1, 2000.

LEGISLATIVE HISTORY

AB 2096 (2000) would provide for a \$500 credit to taxpayers who provide long-term care to elderly individuals who reside with the taxpayer. AB 2281 (2000) would allow 25% of the cost of long-term insurance as a deduction starting in the 2002 tax year and incrementally increasing to 100% beginning in the 2007 tax year.

SPECIFIC FINDINGS

Under **federal law** long-term care services are defined as services necessary to diagnose, prevent, cure, treat, mitigate, rehabilitate and maintain or to provide personal services to a chronically ill individual. A chronically ill individual is generally defined as an individual certified annually by a licensed health care practitioner as being unable to perform (without substantial assistance) at least two of the following activities of daily living (ADLs): eating, toileting, transferring, bathing, dressing and continence or requires substantial supervision to protect such individual from health and safety concerns due to severe cognitive impairment.

Current **federal law** specifically allows a deduction for medical expenses for the unreimbursed expenses for qualified long-term care services provided to the taxpayer, the taxpayer's spouse or the taxpayer's dependents (subject to the present-law floor of 7.5% of adjusted gross income). Amounts received under a long-term care insurance contract (regardless of whether the contract reimburses expenses or pays benefits on a per diem or other periodic basis) are treated as reimbursement for expenses actually incurred for medical care.

Board Position:

<u> </u> S	<u> </u> NA	<u> </u> NP
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<u> </u> N	<u> </u> OUA	<u> X </u> PENDING

Department Director

Date

Alan Hunter for GHG

3/29/00

Long-term care insurance premiums, like medical care insurance premiums, are explicitly treated as medical expenses and are deductible on a graduated scale based on the individual's age before the close of the taxable year.

<u>Age of Individual</u>	<u>Maximum Deduction</u>
40 or less	\$200
More than 40 but less than 50	375
More than 50 but less than 60	750
More than 60 but less than 70	2,000
More than 70	2,500

Current law also excludes from gross income of the employee any employer contributions to accident and health plans, except for contributions to cafeteria plans or "flexible spending arrangements," as defined. In addition, current law excludes from gross income the receipt of benefits from long-term care insurance.

Current **federal law** imposes an information reporting requirement on insurance companies paying long-term care benefits. In addition to the normal reporting requirements (identification of the recipients and amounts paid out by the company), the insurance company also must include the type of policy issued to the recipient. A penalty excise tax may be imposed on issuers of long-term care insurance companies that fail to satisfy the above requirements.

Current **California law** conforms to federal tax provisions related to long-term care.

Federal law allows a \$2,750 (for 1999) exemption (deduction from income) for each dependent of the taxpayer. To qualify as a dependent, an individual must:

- (1) be a specified relative or member of the taxpayer's household;
- (2) be a citizen or resident of the U.S. or resident of Canada or Mexico;
- (3) not be required to file a joint tax return with his or her spouse;
- (4) have gross income below the dependent exemption amount (\$2,750 in 1999) (the gross income threshold test) if not the taxpayer's child; and
- (5) generally receives over half of his or her support from the taxpayer (the support test).

California law conforms to the federal definition of a dependent (items 1 through 5 above.) However, in lieu of a \$2,750 deduction from income, the state allows a credit, \$227 for 1999, that is applied against the taxpayer's tax liability.

This bill would provide a \$500 non-refundable credit for each applicable individual to whom the taxpayer presumably provides long-term care. An applicable individual may be the taxpayer, spouse of the taxpayer, or a qualifying (under this bill) dependent who has been certified to have long-term care needs.

For purposes of this credit, **this bill** would broaden the definition of a dependent in two ways. First, the gross income threshold test would increase to the sum of the federal personal exemption amount, the federal standard deduction, and the additional federal deduction for the elderly and blind (if applicable). In 1999, the gross income threshold would generally be \$7,050 for a non-elderly dependent and \$8,100 for an elderly or blind dependent. The threshold amounts are calculated using the federal amounts.

Second, the support test would be deemed to be met if the taxpayer and an individual with long-term care needs reside together for a specified period. The length of the specified period would depend on the relationship between the taxpayer and the individual with long-term care needs. The specified period would be over half the year if the individual is the parent (including stepparents and in-laws), or ancestor of the parent, or child, or descendant of the child, of the taxpayer. Otherwise, the specified period would be the full year. If more than one taxpayer resides with the person with long-term care needs and would be eligible to claim the credit for that person, then those taxpayers generally must designate the taxpayer who would claim the credit. If the taxpayers fail to do so or if they are married to each other and filing separate returns, then only the taxpayer with the higher modified federal AGI would be eligible to claim the credit.

Under **this bill**, an individual age six or older would be considered to have long-term care needs if he or she were certified by a licensed physician (prior to the filing of a return claiming the credit) as being unable for at least six months to perform at least three ADLs without substantial assistance from another individual, due to a loss of functional capacity (including individuals born with a condition that is comparable to a loss of functional capacity).

A child between the ages of two and six would be considered to have long-term care needs if he or she were certified by a licensed physician as requiring substantial assistance for at least six months with at least two of the following activities: eating, transferring, and mobility.

A child under the age of two would be considered to have long-term care needs if he or she were certified by a licensed physician as requiring for at least six months specific durable medical equipment (for example, a respirator) by reason of a severe health condition or requiring a skilled practitioner trained to address the child's condition when the parents are absent.

As under the present-law rules relating to long-term care, ADLs would be eating, toileting, transferring, bathing, dressing, and continence. Substantial assistance would include both hands-on assistance (the physical assistance of another person without which the individual would be unable to perform the ADL) and stand-by assistance (the presence of another person within arm's reach of the individual that is necessary to prevent, by physical intervention, injury to the individual when performing the ADL).

As an alternative to the 3-ADL test described above, an individual would be considered to have long-term care needs if he or she were certified by a licensed physician as (a) requiring substantial supervision for at least six months to be protected from threats to health and safety due to severe cognitive impairment and (b) being unable for at least six months to perform at least one or more ADLs or to engage in age appropriate activities as determined under regulations prescribed by the Franchise Tax Board (FTB) in consultation with the Secretary of Health and Welfare Agency.

This bill would provide that a portion of the period certified by the physician would have to occur within the taxable year for which the credit is claimed. After the initial certification, individuals would have to be recertified by their physician within three years or such other period as the FTB prescribes.

This bill would require the taxpayer to provide a correct taxpayer identification number for the individual with long-term care needs for which the credit is to be claimed, as well as a correct physician identification number for the certifying physician on the tax return. Failure to provide correct taxpayer and physician identification numbers would be subject to the mathematical error rule. Under that rule, the FTB may summarily assess additional tax due without sending the individual a notice of proposed assessment. Further, the taxpayer could be required to provide the physician certification upon the FTB's request.

Policy Considerations

This credit would not be limited to taxpayers or applicable individuals who reside in California.

This bill would not actually require the taxpayer to provide long-term care to an applicable individual. This bill would only require the applicable individual to be certified as needing long-term care and that the applicable individual be the taxpayer, taxpayer's spouse or a qualifying dependent of the taxpayer.

The proposed FTB regulations to be adopted in consultation with the Health and Welfare Secretary governing physician certification based on one or more ADL or inability to perform age appropriate activity are more properly adopted by that agency. The FTB would the rely solely on the physician's certification.

FISCAL IMPACT

Departmental Costs

This bill would not significantly impact the department's costs.

Tax Revenue Estimate

Revenue losses under the Personal Income Tax Law for a stand-alone state credit are estimated as follows:

Revenue Impact AB 2268 For Taxable Years Beginning 1/1/2000 Assumed Enactment After 6/30/00 (In Millions)		
2000-01	2001-02	2002-03
-\$48	-\$41	-\$45

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this proposal.

Tax Revenue Discussion

The impact of this bill would depend upon the number of taxpayers eligible to claim the credit (estimated to be 158,000), the average credit claimed and the average credit applied against available tax liabilities.

This estimate is based on a proration of the estimate calculated by the U.S. Treasury for a similar federal credit.

Starting with the federal impact on liabilities:

1. The California eligible population is assumed to be 11% of the nation.
2. Because California tax rates and proposed credit are lower than federal tax rates and \$1,000 proposed credit, it is assumed that the credit absorption rate would be 75% of the federal (a greater portion of the calculated credit would not be applied because of insufficient tax liabilities).
3. Because of the absence of income caps, it is assumed that the eligible population would be 7.9% greater than if the caps proposed in federal legislation were applied. This assumption is based on the department's Personal Income Tax model for taxpayers above the federal income caps.
4. For the additional 7.9%, it is assumed that each taxpayer would be able to absorb the full \$500 credit.

BOARD POSITION

Pending.